AmCham EU's response to DG Competition's draft proposal for a revised block exemption for technology transfer agreements and for revised guidelines

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The American Chamber of Commerce to the European Union (AmCham EU) welcomes the opportunity to submit comments to the Commission consultation on the draft proposal for a revised block exemption for technology transfer agreements (TTBER) and for revised guidelines. One of the key themes that runs through AmCham EU's comments to the 2011-2012 consultation, and which also runs through this paper, is the need to ensure that the revised TTBER and guidelines create legal and commercial certainty to parties engaging in technology transfer.

As the draft guidelines recognise, most license agreements create pro-competitive efficiencies as they lead to dissemination of technology and promote follow-on innovation. Despite this general declaration, the Commission's new proposals appear in parts to seek to limit the protection that technology transfer agreements currently enjoy. This could result in less certainty and flexibility for business to license their innovations, which in turn may discourage undertakings from investing in developing new products and processes and may also affect follow-on innovation by reducing licensing.

AmCham EU's comments therefore identify areas where the draft TTBER and guidelines appear unclear or where they challenge the existing accepted practices that have so far not been found to create anti-competitive concerns.

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Background and Analysis

Removal of the safe harbour relating to termination in case of challenge provisions

AmCham EU considers this to be a significant proposed change as it would affect provisions that are standard practice in many IP licenses.

Article 5 (1) (b) of the draft TTBER states that a **termination** of a license agreement **on challenge provisions** shall no longer fall within the safe harbour of the proposed regulation draft. The current regulation permits termination of the technology transfer agreement in the event that the other party challenges the validity of any of the intellectual property rights. **AmCham EU believes that this provision should remain unchanged.** A licensor should be able to respond to a loss of confidence as a result of ex post challenging the validity of intellectual property rights by the licensee.

The proposed change appears to be motivated by the perception that the current exemption allowing the right to terminate in case of a challenge has the same effect as a non-challenge clause. There is also an apparent desire to eliminate invalid IP rights. The guidelines (par. 125) take the view that licensees should retain the possibility of invalidating IP rights if such rights were granted in error. Such an assumption cannot be sustained and is a significant statement that is inconsistent with the pro-IP position of the European Commission. Business must be in a position to rely on the presumption that validly granted IPR can be relied upon. In addition, this assumes that validity is a clear cut situation, which is not the case in practice. Invalidity decisions are often based on facts that were not known or available to the owner of the IP rights at the time the rights were granted.

As a matter of principle, prospective licensees are at liberty to assess the validity of the IP rights at the time of execution of the license agreement. Indeed, the draft guidelines notes in paragraph 123 that the licensee is 'normally in the best position to determine whether or not an intellectual property right is invalid'.

In the absence of a right for the licensor to terminate the license in case of challenge, it can be expected that some licensees would attempt to challenge the validity of IP right ex post in an attempt to enforce a change in the commercial terms of the license (e.g. to decrease the royalties in case of an unforeseen commercial success). It would be odd if the result of the proposed change was to incentivise the threat or litigation as a means of renegotiating contracts freely entered into. However, in order to create a level of certainty, such issues are usually – and best - addressed in the drafting of the license when it is concluded and not through a challenge of the IP rights. This proposal could even encourage potential infringers of IP rights to take a license before launching an attack on such IP right as there is then no downside to attacking the IP right.

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There is therefore a significant likelihood that the suggested reforms will create greater uncertainty for companies.

It would be unreasonable and disproportionate to expect a licensor to continue a license under such circumstances and this would indeed go against basic principles of civil law of most Member States. If a licensee attacks the foundation of the license, this changes the very essence of the contract that has been concluded and a licensor should be able to terminate the license.

It would indeed be unfortunate if the revised TTBER and guidelines resulted in licensors being more reluctant to license technology and for (unwarranted) IP litigation to increase if this proposal would be adopted.

Further, such clauses rarely restrict competition and play an important role in facilitating the dissemination of technology. There are already sufficient safeguards to ensure that courts and competition authorities can intervene in those rare cases in which such clause could have anticompetitive effects. Indeed, given that such clauses are only relevant in the context of litigation, Member State courts should be free to consider the validity of such clauses within the overall context of the license and the market. This is notably true where the validity and infringement of the right is at issue, a question that antitrust authorities are not competent to address. The exclusion of non-challenge clauses from the safe harbour enables courts to play this role.

Termination clauses are very common and the proposed change risks opening up new and existing licenses agreements to challenge. It also shifts the balance between licensors and licensees that was established by the current rules where only non-challenge clauses are excluded from the safe harbour.

Field of use restrictions

AmCham EU agrees with paragraph 197 of the draft guidelines, namely that 'field of use restrictions may have procompetitive effects'. As AmCham EU stated in its submission of 3 February 2012, field of use is 'among the most critical license terms because [it] allow[s] licensors to avoid having to choose between licensing their entire intellectual property right and nothing at all. Rather than restrict the licensee's commercial freedom, such provisions increase it'.

Paragraph 194 of the draft guidelines indicates that field of use 'must be defined objectively by reference to identified and meaningful technical characteristics of the contract product'. This approach appears too restrictive, as it places types of field of use license grants, which cannot be defined precisely in technical terms, outside the block exemption and, presumptively, within the category of hardcore restraints. Such types of field of use license grants do not necessarily allocate customers and may be pro-competitive.

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In light of the above, the guidelines should make it clear that non-technical fields of use that are narrower than a product market do not constitute hardcore restraints. In this respect, AmCham EU respectfully regrets the restrictive way in which paragraph 193 delineates the term 'industrial sectors'. It states that '[a]n industrial sector may encompass several product markets but not part of a product market'. This amendment would confirm that restrictions based on non-technical fields of application within the same product market are presumptively hardcore restraints. As stated, this would inhibit license grants that may be pro-competitive. The negative effect on licensing activities is compounded by the inherent difficulty in determining what constitutes a 'product market'.

Even if paragraph 194 of the draft continues to define 'field of use' by reference to technical characteristics only, it should be clarified that such characteristics are not limited to the 'contract product', i.e. the product incorporating or produced with the licensed technology. 'Contract products' can be either final or intermediate products. In the latter case, the guidelines clarify that licensors are allowed to delineate their license grants on the basis of the technical characteristics of the end product into which the 'contract product' is incorporated.

AmCham EU does not support a proposal to subject all exclusive grant backs to individual assessment irrespective of whether improvements are severable

Article 5 (1) (a) provides that any **exclusive grant back** clauses are outside of the safe harbour of the proposed draft regulation. Currently, only obligations on the licensee to grant an exclusive license on own severable improvements are outside the safe harbour. Thus, exclusive grant back clauses regarding to non-severable improvements are allowed under the current regulation. **AmCham EU considers that the current position should remain unchanged.**

AmCham EU questions the reduction of market share threshold for competing licensee as regards to in-house production

AmCham EU questions whether this is necessary and whether it will simply reduce flexibility without adding benefit to the protection of competition.

The current proposal could have the effect of discouraging parties who are the only parties active in a particular technology area from benefitting from exchanges of technology that would allow them to progress the technology in a pro-competitive way.

AmCham EU considers that the licensing of software copyright should be subject to the TTBER and not general distribution rules or the Vertical Block Exemption Regulation

AmCham EU does not think there is a need for aligning more closely the TTBER and the Vertical Block Exemption Regulation (VBER). Both regulations serve very different purposes that are based on the different nature of technology and products or services. The European approach to technology transfer licences reflects the view that most such licences are pro-competitive, leading to the dissemination of technology and encouraging follow-on innovation. Certain limitations on the behaviour of licensees in connection with the licensed technology are accepted as creating either or both of general economic benefits or benefits for consumers. For the licensing of technology, this flexibility is necessary to commercially exploit the technology and provide sufficient incentives for innovation. The same applies to the licensing of software.

The existing TTBER and guidelines apply to technology transfers pursuant to which software is exploited for the production of goods and services, referred to as 'contract products'. Licensed technology may be exploited by incorporating it into a contract product or by using it in a production process. By contrast, agreements relating to the supply of software for resale (where the distributor does not acquire a licence to any rights in the software but only has the right to resell the copies), are agreements for the resale of goods. The latter are vertical distribution agreements falling within the Vertical Restraints Block Exemption Regulation and related guidelines.

Reflecting the economics of technology licensing, the TTBER and guidelines afford favourable treatment to restraints in licences that should also apply to software licenses. As the guidelines note:

> Most licence agreements do not restrict competition and create procompetitive efficiencies. Indeed, licensing as such is pro-competitive as it leads to dissemination of technology and promotes innovation. In addition, even licence agreements that do restrict competition may often give rise to pro-competitive efficiencies, which must be considered under Article 101 (3) and balanced against the negative effects on competition. The great majority of licence agreements are therefore compatible with Article 101.

Scrutiny to assess no-challenge clauses of settlement agreements

The proposed guidelines provide that non-challenge clauses in settlement agreements may be anticompetitive under specific circumstances, giving the example of the case 'where the licensor knows or could reasonably be expected to know that the licensed technology does not meet the respective legal criteria to receive intellectual property protection, for example where a patent was granted following the provision of incorrect, misleading or incomplete information' (par. 227).

These provisions appear to be a consequence of the pharmaceutical sector inquiry launched in 2009 by the Commission. Unfortunately, the proposed revision of the guidelines is very broad and goes well beyond the current scrutiny in the context of the pharmaceutical industry.

Application of Article 101 to non-challenge clauses when the licensor knows that the licensed technology does not meet the respective legal criteria to receive intellectual property protection seems uncontroversial. By contrast, it is in our view problematic to extend this rule to cases where the licensor could reasonably be expected to know. This latter standard is vague and risks unduly opening the door to ex post challenges of the very intellectual property rights that were at the centre of the dispute covered by the settlement. It thereby risks creates disincentives to settle costly litigation.

The proposed language seems to be inspired by the AstraZeneca case where the General Court found that AstraZeneca 'could not reasonably be unaware' that its conduct was misleading. However, when describing AstraZeneca's conduct in view of the facts, the European Courts used terms such as 'highly misleading', 'deliberately attempted to mislead' and 'knowingly accepted'. Thus we believe that it is perfectly possible to create a rule limited to cases where the licensor 'knows' with the case law.

Assessing after the fact whether the licensor could reasonably be expected to know that its IP rights should not have been granted at the time of grant, can only lead to second guessing and leaves little room for a fair assessment of the facts as they would have appeared to be at the time of granting those rights. This is not a test that should be applied broadly, if at all. It is wholly reasonable as a matter of public policy that IP are allowed to rely on the IP granted by the relevant office, so long as it was not obtained through fraud on the system. Such instances are rare and are covered by well-known case law. For the guidelines to seek to establish more general principles is unnecessary at best.

The guidelines should be revised and limit the discussion to situations where there is evidence (court decision) that the patent owner attempted to mislead the patent office.

AmCham EU considers that it is also problematic that the guidelines state that scrutiny of non-challenge clauses is necessary 'if the licensor induces, financially or otherwise, the licensee to agree not to challenge the validity of the technology' (par. 227). AmCham EU considers this rule too vague and risks enabling parties to unduly reopen settlements by challenging the intellectual property rights that are the very subject matter of the settlement. Settlements very often involve an exchange of value between the parties and such value is exchanged in order to achieve a settlement. For instance, the parties may cross-license or transfer intellectual property rights as part of the settlement. Since non-challenge clauses are inherent to settlements it would seem to be a simple matter for a party to argue that it is being induced not to challenge the validity of licensed technology opening the door to challenging validity in great many cases despite the settlement.

Revised guidance on technology pools

The draft guidelines expand the current competitive assessment of technology pools. While some clarification of the Commission's position in the application of antitrust policy to technology pools is welcome, the current structure of the safe harbour in the draft guidelines may not sufficiently address all relevant circumstances. Further thought should be given to the scope of the safe harbour. This is particularly so given that the working principles for technology pools are very much works in progress and it is difficult to draw conclusions whether a particular refusal to license should be problematic on competition law terms. Such issues are most appropriately dealt with in the context of the Horizontal guidelines.

In order to benefit from the safe harbour, the draft guidelines suggest applying the concept of Fair, Reasonable and Non-Discriminatory (FRAND) terms to the licensing of essential technology. The draft guidelines refer back to the guidelines Horizontal Co-operation Agreements (GHCA) for a description of FRAND. However, it is confusing to apply the GHCA notion to all patent pools. Pools comprising standards-essential patents raise particular issues that should not be transposed to other pools. Firstly, the FRAND commitment referred to in the GHCA is not mandatory and relates to safe harbour conditions set out in the GHCA. Secondly, the GHCA FRAND context is that the FRAND commitment is a voluntary commitment given bilaterally by a standards essential IP holder to the standards body as a condition for inclusion in the standard. Applying the GHCA FRAND to pools is therefore unnecessary, as where pools are created under formal standards the essential IP holders will likely have made FRAND commitments. AmCham EU considers that this suggestion is not workable especially given that the draft guidelines already recognise that pools can be formed in a non-standards context. The reference to the GHCA should therefore be removed; the current guidelines refer to FRAND licensing, as commonly understood by commercial courts. This should be maintained.

Passive sales restrictions

AmCham EU considers that the rules on passive sales constitute a material tightening of the regime, which may not always be appropriate. The Commission maintains that this aims to harmonise its approach with the VBER and the updated guidance. However, such an approach may fail to take into account the particularities of products and markets and is likely lead to inconsistencies. Therefore, AmCham EU considers that this harmonisation effort is not appropriate in this context.

AmCham EU considers this adds unnecessary restrictions and fails to recognise differences between general distribution and technology licensing. AmCham EU is also concerned that this will undermine and/or reduce licensing of technology.

Article 102 considerations

AmCham EU notes that the guidelines discuss 102 concerns in a number of paragraphs (e.g. paras. 78, 165, 170 [footnote 76] and 251). In order to set the relevant tone and context and avoid confusion on the part of businesses, national agencies and courts with regard to controlling law, AmCham EU believes that the guidelines should at least refer to the case law of the Court of Justice that sets out the limits and conditions under which antitrust intervention is permitted.

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AmCham EU speaks for American companies committed to Europe on trade, investment and competitiveness issues. It aims to ensure a growth-orientated business and investment climate in Europe. AmCham EU facilitates the resolution of transatlantic issues that impact business and plays a role in creating better understanding of EU and US positions on business matters. Aggregate US investment in Europe totalled €1.9 trillion in 2012 and directly supports more than 4.2 million jobs in Europe.

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